



Illinois Department of Revenue

Spring 2016 Legislative Agenda

Omnibus Proposals

1. Fraud Prevention Package.....page 3
2. Sales Tax Package.....page 5
3. Technical Clean-up Packagepage 7

Standalone Proposals

4. Cook County PVUT Collection.....page 10
5. Local Tax Administration Fee.....page 12
6. Taxpayer Confidentiality.....page 13
7. Statewide Tax Lien Registry.....page 15
8. Sales and Excise Tax Refund Fund.....page 16
9. Verified Overpayment Language.....page 17
10. Pay Use Tax Disbursements from a Non-Appropriated Account.....page 18

OMNIBUS FRAUD PREVENTION PACKAGE

Summary:

- a. **Work with banks to recapture fraudulently paid refunds by giving IDOR the authority to enter into agreements with banks that facilitate the recovery of fraudulent refunds.**
- b. **Mandate an electronic W-2 Filing Deadline**

Bank Indemnification

Fraudulent refund claims are a growing problem in tax administration at both the state and federal levels. IDOR is always exploring ways to identify and prevent fraud. One common scheme is when an identity thief applies to the taxing agency for a refund under someone else's name, and requests that the refund be electronically deposited in a bank account controlled by the identity thief. IDOR works to identify these bank accounts and the bank will then freeze the account. In these cases, banks are willing to turn over the funds to IDOR, but only if IDOR signs an agreement assuring the bank that it will be reimbursed if it is later discovered that the refund was not obtained by fraud. IDOR does not currently have this authority.

In IDOR's discussion, banks have noted that this issue will continue to come up as banks become more sophisticated in detecting fraudulent activities. The banks are willing to freeze accounts that are fraudulent, but want some legal protection before releasing the funds to the rightful owner. This proposal also would add a statutory provision that a person in possession of funds upon which a tax levy was made can discharge any obligation with respect to the funds upon surrendering those funds. Ohio, Indiana, Kentucky and Wisconsin all provide letters of indemnification for banks.

- **Fiscal Impact:** none
- **Previously Submitted:** SB 1786 (Spring 2015)

Filing Deadline Mandate for W-2's

Mandate businesses to electronically file W-2s by February 15; do not issue individual refunds until March 1 so as to provide a window to compare individual withholding to business W-2s—this delay would afford the Illinois Department of Revenue (IDOR) time to evaluate the IL-1040 Illinois Individual Income Tax Returns and associated Wage and Tax Statements (W-2) to determine their validity by subjecting them through a logical sequence of tests, before refund payments are issued. These tests would include proven business rules, historical data, and the incorporation of external sources. Historically, refunds have been issued before the Department had access to its sources that help detect fraud. Delaying refunds until the first week of March would facilitate our efforts and give us access to invaluable resources, thereby preventing erroneous/fraudulent refund payments from being issued.

- **Fiscal Impact:** none
- **Previously Submitted:** N/A

OMNIBUS SALES TAX PACKAGE

Summary:

- a. **Create a Sales Tax Exemption for retailers who sell to federally exempt entities**
 - b. **Amend the Statute of Limitations for a timely filed Retailers Occupation Tax Return**
-

Sales Tax Exemption for retailers who sell to federally exempt entities

Create an Retailers Occupation Tax /Service Occupation Tax exemption for sales to organizations exempted from Use Tax by federal law: amend Retailers Occupation Tax Act, 35 ILCS 120/2-5(16), which currently reads: “Petroleum products sold to a purchaser if the seller is prohibited by federal law from charging tax to the purchaser”—and broaden it to include all types of tangible personal property. To have the purchaser exempt from Use Tax, while the retailer is taxable, is an anomaly under our complementary sales tax system and creates administrative burdens on retailers. A corresponding amendment should be made to add similar verbiage to the Service Occupation Tax Act.

Federal law exempts certain quasi-governmental agencies such as Amtrak, federal credit unions, and Fannie Mae from paying Use Tax on their purchases. There is no corresponding exemption, however, for the retailer. So the retailer is obligated to pay the ROT on the transaction since the incidence of the tax is on the occupation of selling; however, they are not allowed to collect from the customer the corresponding use tax.

Illinois taxes the retail sale and use of tangible personal property under two separate but related statutes. The Illinois Retailers' Occupation Tax Act, 35 ILCS 120/1 et seq. (1994 State Bar Edition), imposes a tax on Illinois retailers measured by a percentage of their gross receipts from sales for use or consumption. The Illinois Use Tax Act, 35 ILCS 105/1 et seq. (1994 State Bar Edition), imposes a tax on the purchaser by taxing the use of tangible personal property purchased from a retailer. When a purchase is made from an Illinois retailer (a seller who accepts purchase orders in Illinois or who fills orders from an Illinois inventory), both taxes are applicable and are complementary. That is, the Illinois retailer incurs Retailers' Occupation Tax liability on gross receipts from the sale and reimburses himself by collecting the Use Tax from the customer and retaining it.

Because there is currently no exemption from ROT/SOT for retailers who sell to federally exempt entities, the retailers must then remit ROT without the ability to collect the corresponding Use Tax. There is, however, an exemption in the ROT for petroleum products sold to purchasers if federal law prevents the seller from charging tax to the purchaser. This is very narrow and only includes petroleum products.

Amend the Statute of Limitations for a timely filed Retailers Occupation Tax Return

Amend the Retailers Occupation Tax Act to state that the statute of limitations is based on when the return is due as opposed to when receipts are received in order to make all four sales tax acts consistent.

Currently, the Retailers Occupation Tax Act calculates the statute of limitations for timely filed returns based on when receipts from sales are received, but Service Occupation Tax, Use Tax, and Service Use Tax begin the statute of limitations when returns are due.

The result of the inconsistency is that the earlier statute of limitations causes the Retailers Occupation Tax due on June and December return to be uncollectable 6 months before the Service Occupation Tax, Use Tax, and Service Use Tax when all four taxes are reported on the same return (Illinois ST-1 return).

This creates an inconsistency in statute that is functionally impossible to administer for processing purposes when all four taxes are currently reported on the same return.

Fiscal Impact:

Previously Submitted: No

OMNIBUS TECHNICAL CLEAN-UP PROPOSAL

Summary:

- a. **Adjust the deadline for the Unified Economic Development Budget**
- b. **Raise the Cigarette Use Tax Penalty**
- c. **Effective Date Revisions**

Adjust the deadline for the Unified Economic Development Budget

This is an attempt to address repeated audit findings the Department of Revenue incurs due to the Department not having the data necessary to file the Unified Economic Development Budget report by the deadline mandated in statute.

20 ILCS 715/10 requires IDOR to produce a report three months after a fiscal year ends on the economic development incentives from returns filed during the prior fiscal year. IDOR is only able to file a Unified Economic Development Budget submission to the General Assembly and DCEO for older fiscal years, rather than the detailed information for the immediately preceding fiscal year required by statute.

The Department is unable to file a report that contains preceding fiscal year information largely due to the fact that many corporations elect to file by the late filing deadline. This proposal would simply extend the deadline for this report by three months so that the data required to complete it is available.

Raise the Cigarette Use Tax Penalty

The Cigarette Tax Act (35 ILCS 130/1) and Cigarette Use Tax Act (35 ILCS 135/1) each allow the Department to impose penalties on persons that possess contraband packages of cigarettes. The most common type of contraband cigarettes are packages that do not contain an Illinois tax stamp or contain a tax stamp from another state. The civil penalties imposed under the Cigarette Tax Act and the Cigarette Use Tax Acts were raised several years ago. Under the Cigarette Tax Act (Section 18b) and Cigarette Use

Tax Act (Section 25a), a person possessing more than 100 packages of cigarettes is subject to a penalty of \$25 for each package of cigarettes in excess of 100 packages.

Under the Cigarette Use Tax Act (Section 25b), a person possessing not more than 100 packages of cigarettes is subject to a penalty of \$20 for each package of cigarettes, and under the Cigarette Tax Act (Section 18c), a person possessing not more than 100 packages of cigarettes is subject to a penalty of \$10 for each package of cigarettes.

For reasons unknown (likely an oversight), the penalty in Section 18c of the Cigarette Tax Act was not increased to \$20 to make the penalty consistent with the Cigarette Use Tax Act.

Effective Date Revisions

Revise the timeframes for when IDOR must implement new local Automobile Renting Retailers Occupation Tax and Automobile Renting Use Tax rate changes so that the implementation is on the same schedule as other local taxes (i.e. begin collection on January 1 for ordinances filed with IDOR on or before the previous October 1 and begin collection on July 1 for ordinance filed w/ IDOR on or before the previous April 1).

There are currently conflicting timeframes for ART Retailers Occupation Tax and ART Use Tax.

Currently the municipal Automobile Renting Tax ROT statute (65 ILCS 5/8-11-7) provides that, “An ordinance or resolution imposing a tax hereunder or effecting a change in the rate thereof shall be effective on the first day of the calendar month next following publication as provided in Section 1-2-4.”

The local Automobile Renting Tax UT statute (65 ILCS 5/8-11-8) says that it takes effect “on the first day of the second calendar month next following publication. We do not know any logical reason for the different timeframes

The differing timeframes pose two problems for IDOR. One problem is that, in either case, the turnaround for IDOR to implement this new local tax, including notifying renting companies and updating the system is very short – max is 30 days – but could be much shorter. The other problem is that technically a one-month delay to implement

the local Automobile Renting Tax-UT. These liabilities are reported on the same return and the processing system is not set up to require the ROT but not the UT to be filed for that first month.

Our proposal is to make this local tax just like the others (e.g. home rule and non-home rule sales tax; county public safety and county school facility sales tax). Adopt and file an ordinance on or before April 1 and the Department will implement (for both ART-ROT and ART-UT) on July 1; or adopt and file an ordinance on or before October 1 and the Department will implement (for both ART-ROT and ART-UT) on January 1.

This addresses both the unreasonably quick implementation (which can be burdensome on both rental companies and IDOR and increases the likelihood for error) as well as the misaligned beginning date for both taxes at the same time.

Note that the County ART taxes (55 ILCS 5/5-1032 and 5-1033) do not have the staggered effective date, but do require immediate implementation.

Fiscal Impact: None

Previously Submitted: No

COOK COUNTY PVUT COLLECTION

Amend the Local Tax Collection Act (35 ILCS 720/1) to make changes to conform it to other local taxes and to direct the administrative fee to Tax Compliance and Administration Fee (TCAF) rather than the General Revenue Fund (GRF). The Local Tax Collection Act allows IDOR to collect Cook County's and Chicago's private vehicle use tax.

Background

On October 31, 2014, IDOR signed an Intergovernmental Agreement (IGA) with Cook County (signed by Cook County on December 1, 2014) that provides for IDOR to collect Cook County's Private Vehicle Use Tax (PVUT) beginning on July 1, 2015. IDOR entered into a substantially similar IGA with the City of Chicago on June 8, 2015.

IDOR relied upon the authority given to it in the Local Tax Collection Act to collect the PVUT for Cook County and the City of Chicago. The Local Tax Collection Act does not require IDOR to collect any taxes on behalf of local governments, but instead allows IDOR to enter into an agreement with a local government to collect a tax that is similar to that of a tax imposed by IDOR.

The Local Tax Collection Act provides for an administrative fee of 2% to be deposited into GRF. The parties negotiated legislative changes that would, among other things, provide for IDOR to collect a 5% administrative fee that would be deposited into the Tax Compliance and Administrative Fund, which could then be used by IDOR to offset its costs associated with the collection of the PVUT. The parties negotiated draft legislative language that was attached to the IGA as an exhibit. The IGA required the County and the City to both pursue enactment of the legislation, and IDOR agreed to support the legislation. In an effort to keep pressure on the County and the City to have continued incentive to pass the legislation, the IGAs provide that in the event the legislation is not enacted by May 31, 2016, the IGAs will automatically terminate.

There are three primary reasons why it is urgent to pass the legislative changes that were agreed to by and between IDOR, Cook County and the City of Chicago:

1. The administrative fee being retained for collecting the PVUT is currently limited to 2%, even though the parties all agreed that the administrative fee would be 5%. This is because current law limits the administrative fee to 2%, but the proposed changes would add language that would allow the parties to negotiate a fee greater than 2%.
2. The administrative fee is intended to offset IDORs cost to collect the PVUT for the local governments, but the current statute provides for the money to be deposited into GRF, so IDOR never actually gets to apply the fee to its costs. The proposed changes would provide that the administrative fee be deposited into the Tax Compliance and Administrative Fund, which would allow IDOR to use it to cover its costs.
3. Pursuant to their own terms, the IGAs will terminate automatically in the event the legislation is not enacted by May 31, 2016.

Fiscal Impact: During fiscal year 2016 we have collected an average of \$1,728,335 per month for these two local governments' private vehicle use taxes. Fiscal Year 2016's projected total collection for these taxes is \$20,740,020. A 2% administrative fee would equate to \$414,800 annually. A 5% administrative fee would equate to \$1,036,980 in FY16. The 2% administrative fee would be in line with the Department of Revenue's actual costs to administer these taxes. *Depositing the administrative fee into the TCAF would enable the Department of Revenue to utilize the administrative fee to pay its costs in administering these taxes on the behalf of Cook County and the City of Chicago. Depositing the administrative fee into the General Revenue Fund would not directly provide funding to the Department of Revenue for the efforts it expends to administer these tax types for Cook County and the City of Chicago.*

- **Previously Submitted:** SB 1236 HA1 (with additional confidentiality language)

LOCAL TAX ADMINISTRATION FEE

In recent years, IDOR has been asked to provide increasingly more services via inter-agency agreements to other state and local government agencies. The legislative change IDOR is seeking would permit the reimbursement received from the state or local government agency (prescribed via inter-agency agreement) to be deposited into the Tax Compliance and Administration Fund (TCAF). The deposit into TCAF would then be utilized, subject to appropriation, to fund IDOR's on-going operational expenses to provide services prescribed via inter-agency agreement. Without this reimbursement, IDOR is forced to use its tax administration appropriations to perform tasks for other state and local government agencies.

IDOR administers 76 state and local tax laws. For many of the local taxes, an administrative fee is imposed and deposited into the TCAF to reimburse IDOR for its efforts to administer the tax on behalf of the local government. Currently, there are 11 local taxes IDOR administers but receives no administrative fee. IDOR distributed over \$8.5 billion to local governments in FY 15.

- **Fiscal Impact:** approximately \$58 Million dollars (FY 17 projections at a standard 2% fee rate) subject to appropriation which would not constitute additional funding for the Department. The Department is currently providing these administrative services to local governments free of charge and paying for the costs of administration through the regular appropriation request.
- **Previously Submitted:** N/A

TAXPAYER CONFIDENTIALITY

Cash-strapped units of local government across Illinois are under more pressure than ever to stabilize expenses. In hopes of augmenting revenue, certain jurisdictions are contracting with private, third-party audit firms, often via contingent fee arrangements. IDOR has the singular interest in ensuring the proper collection, remittance and allocation of tax from and to the correct unit(s) of local government. The Department's local government division works closely with counties and municipalities and is always happy to assist units of local government with any tax allocation or distribution concerns, free of charge.

- Contingent fee arrangements threaten taxpayer confidentiality and undermine the voluntary compliance system, a fundamental principle of U.S. tax administration. Contingent fee auditors have an incentive to interpret the law in an unfairly aggressive manner and to not inform taxpayers of overpayments. Contingent fee arrangements divert large amounts of tax dollars away from units of local government through contracts that require that the consultant keep high percentages of “found” dollars as payment for their service.
- If local jurisdictions continue to contract with third-party consultants, IDOR's ability to obtain federal tax information from the IRS—critical to the proper enforcement of the state's tax provisions—may be jeopardized.
- Taxpayer information disseminated to third parties may be misused in a predatory effort to generate profit. Unlike IDOR, third-party consultants are motivated by their own financial interests, which in practice subverts basic standards of impartiality.
- Third-party consultants could exploit ambiguity in the law to encourage units of local government to make frivolous claims for the re-apportionment of tax dollars. Sales tax sourcing issues have been an ongoing problem for units of local government and IDOR is concerned that the involvement of third-party consultants could unnecessarily expand sourcing conflicts, leading to more (costly) litigation.

- Taxpayers have little to no assurance that third-party auditors will adhere to the same privacy standards as those enforced by state and local government employees. Potential risks include identity theft, fraud, corporate exploitation of information to unfairly gain a competitive advantage, solicitation, or data-mining.
- Few states allow private contractors to access confidential tax return information at the state or local level; several states have passed or proposed legislation that prohibits third-party audits. Not surprisingly, the three states that do permit third-party audits happen to be ranked the first, second and third “worst for tax administration” by the Council on State Taxation.

Department position: protect confidential taxpayer information by prohibiting units of local government from allowing private, third-party contractors from accessing confidential taxpayer information provided to units of local government by the Illinois Department of Revenue.

- **Fiscal Impact:** No cost to the state. IDOR would save administrative costs incurred from verifying/dismissing private auditor claims. No cost to local governments. Tax allocation and verification services are already provided free of charge by IDOR to units of local government.
- **Previously Submitted:** SB 1236 HA 1

STATEWIDE TAX LIEN REGISTRY

Currently, statutes require IDOR to file liens with the various county recorder offices throughout the state. Each county recorder charges the State their respective filing and recording fees. IDOR incurs well over \$500,000 annually in recording fees that could be eliminated if we changed the statute to create an in-house tax registry where IDOR recorded and housed tax liens. This would eliminate all cost to the state and allow IDOR to file more liens, thus protecting the collectability of delinquent tax debt. This change would also be more user friendly as all tax liens would be in one location. IDOR response time to lien releases would be expedited as there would be no waiting on county recorders to file a release.

- **Fiscal Impact:** potential \$500,000 net gain for the state and net loss for counties.
- **Previously Submitted:** N/A

SALES AND EXCISE TAX REFUND FUND

IDOR has received hundreds of complaints since the beginning of the fiscal year from frustrated taxpayers who cannot obtain a refund of their overpaid sales tax. These taxpayers cannot get a refund because IDOR did not receive an appropriation to pay sales tax refunds. Even had we received an appropriation, year after year the appropriation is not enough to cover refunds, and we typically run out of our appropriation even when we limit refunds to those who show hardship. Every year, IDOR fields calls from angry taxpayers who cannot understand why they cannot get a refund of their overpaid taxes.

The intent of this proposal is to replace the current appropriation out of GRF for hardship refunds for sales and excise taxes, and instead divert a very small percentage (we calculate 0.18%*) of sales tax receipts into a sales tax refund fund, which would be used to pay sales tax refunds. Mirroring how income tax refunds are currently handled, an agreed to percentage would be deposited in the fund to pay sales tax refunds as claims come in; going forward, this would fix the current problem resulting from the lack of an appropriation, as well as the problem of receiving an underfunded appropriation.

- **Fiscal Impact:** no fiscal impact to state

**Based on our recommended \$15 million refund fund amount and our state sales tax forecast for FY17, the refund fund percentage should be 0.18% for FY17. This assumes the 0.18% is applied to all of the state's 80% share of the 6.25%, including the parts for Build Illinois, Capital, Clean Air, and McCormick Place. We also assume that McCormick Place will get the same amount they received in each of the last two years, \$36.7 million (they could receive more). The amounts refunded (averaging at \$15 million beginning in FY 15) represent hardship refund requests. The amount in the fund will increase proportionately as sales tax receipts increase statewide in subsequent years.*

- **Previously Submitted:** SB 220 (BIMP-2014), SB 1732 (2015)

INCORPORATE VERIFIED OVERPAYMENT LANGUAGE INTO THE EXCISE TAX ACT

Unlike sales taxes, taxpayers who overpay their excise taxes cannot use the overpayment toward a future liability without first applying to have the overpayment converted to a credit. This creates unnecessary paperwork and delays in making the overpayment available for use by the taxpayer. By following the same procedures that currently exist for sales tax overpayments, we can reduce paperwork and make the process more efficient for both IDOR and taxpayers, by allowing excise tax filers to apply credits toward their future liability without filling out burdensome paperwork.

- **Fiscal Impact:** none
- **Previously Submitted:** SB 1804 (Spring 2015)

PAY USE TAX DISBURSEMENTS FROM A NON-APPROPRIATED ACCOUNT

This proposal would allow IDOR to distribute use tax and video gaming disbursements from a non-appropriated fund.

These funds are distributions to units of local government similar to Personal Property Replacement Tax which is a non-appropriated fund.

- **Fiscal Impact:** TBD
- **Previously Submitted:** N/A